

ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author: Strickland Analyst: Kristina North Bill Number: AB 287
Related Bills: See legislative history Telephone: 845-6978 Introduced Date: 2/4/1999
Attorney: Doug Bramhall Sponsor: _____

SUBJECT: Agricultural Product Donations Credit

SUMMARY

Under the Personal Income Tax Law (PITL) and the Bank and Corporation Tax Law (B&CTL), this bill would provide an unlimited 100% credit equal to the wholesale value of agricultural products donated by a farmer to a nonprofit charitable organization or food bank.

EFFECTIVE DATE

This bill would apply to taxable and income years beginning on or after January 1, 1999.

LEGISLATIVE HISTORY

AB 196 (1997/1998); SB 38 (Stats. 1996, Ch. 954); AB 364 (1995/96); AB 2869 (1991/92); AB 2346 (Stats. 1989, Ch. 1248)

PROGRAM HISTORY

AB 2346 (Stats. 1989, Ch. 1248) authorized a similar credit under the PITL and the B&CTL, granting a credit equal to 10% of defined costs, for the donation of agricultural products to certain nonprofit charitable organizations. That credit expired December 1, 1992.

SPECIFIC FINDINGS

Under current federal and state laws, generally all ordinary and necessary expenses of a trade or business are deductible as direct business expenses. For taxpayers required to use an inventory system, certain business expenses are deducted as part of the costs of goods sold.

Under current federal and state laws, a taxpayer may claim a deduction for charitable contributions made to a qualified organization. A charitable contribution is a gift given to or for the use of a qualified organization. It may be in the form of money or property or unreimbursed out-of-pocket expenses incurred by the taxpayer for services rendered to the organization.

For a charitable gift of ordinary income-type property, the amount considered contributed (the property's fair market value [FMV]) must be reduced by the amount of ordinary income or short-term capital gain that would have been recognized if the property had been sold by the donor for its FMV.

Board Position:

_____ S	_____ NA	_____ NP
_____ SA	_____ O	_____ NAR
_____ N	_____ OUA	_____ X PENDING

Department Director

Date

Gerald Goldberg

3/19/1999

Ordinary income-type property is property which would have resulted in some amount of gain, other than long-term capital gain, if sold at its FMV on the date it was contributed.

Current state law also provides a credit equal to 50% of the transportation costs paid or incurred for transporting any donated agricultural product to a nonprofit charitable organization.

Under the Food and Agriculture Code (F&AC), a person engaged in the business of processing, distributing or selling agricultural products may donate food to a nonprofit charitable organization. Agricultural products include fowl, animal, vegetable, or other stuff, product, or article that is customary or proper food for human beings.

This bill would allow a credit equal to the FMV at wholesale of agricultural products donated by a farmer during the taxable or income year to a nonprofit charitable organization or food bank.

This bill would allow a taxpayer to carry over any excess credit until the credit is exhausted.

Since this credit does not specify otherwise, the general rules in state law applicable to the division of credits would apply, and this credit would not reduce regular tax below tentative minimum tax for purposes of alternative minimum tax.

Policy Considerations

This bill would provide an unprecedented, unlimited 100% credit. In addition, taxpayers claiming the credit could also deduct on their federal and state return the value of the agricultural products as a charitable contribution, subject to limitations described above. In effect, the general fund would finance the purchase, at wholesale price, of agricultural products a farmer chooses to donate to charity, while at the same time the farmer would be allowed a charitable contribution for the donation.

Generally, credits are computed as a percentage of a taxpayer's costs. This credit is proposed based on wholesale value, which may be well in excess of cost.

This bill does not specify a repeal date or limit the number of years for the carryover. Credits are typically enacted with a repeal date to ensure that the Legislature reviews its effectiveness. However, once a repeal date has been added and unlimited carryover is allowed, the department would be required to retain the carryover on tax forms indefinitely. Recent credits have been enacted with a carryover limit since experience shows credits are typically used within eight years of being earned.

This bill does not limit the donation to nonprofit organizations or food banks located in California or to California farmers.

Implementation Considerations

The following implementation concerns have been identified.

- ◆ Definitions are needed for "agricultural products," "nonprofit charitable organizations," and "food bank." The author may wish to consider using the definitions provided in the California Food and Agricultural Code regarding the donation of food.
- ◆ It is unclear whether the author intended to include farming co-ops among qualified taxpayers.
- ◆ It is unclear what constitutes "fair market value at wholesale," and a definition would avoid disputes between taxpayers and the department. For example, is it unclear if the market value should be calculated as of the time of donation or at the highest wholesale price of the year.
- ◆ This bill does not provide a process by which the donation of an agricultural product to a nonprofit charitable organization or food bank could be verified. Most credits require some method of verification, such as requiring the recipient organization to provide a written receipt with the type and quantity of product donated, name or names and of the donor or donors, the name and address of the recipient. The receipt should be available to the department upon request.

Department staff is available to assist in resolving these and any other issues that may be identified.

FISCAL IMPACT

Departmental Costs

With the resolution of the implementation concerns, this bill should not significantly impact the department's costs.

Tax Revenue Estimate

Revenue losses could be as high as \$10 million annually, beginning in 1999/2000.

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

Tax Revenue Discussion

The revenue impact for this bill will be determined by the wholesale value of agricultural products donated by farmers to charitable organizations and the amount of credits that can be applied against available tax liabilities. Since wholesale values fluctuate throughout the year, it is assumed the bill as written would allow farmers to claim the highest value during the tax year, not the wholesale value of the actual goods donated at the time of the donation.

It is assumed that the transporting of usable, packaged goods (i.e. fruits, nuts, vegetables, rice, etc.) by farmers, co-ops, or by tax-exempt entities themselves would not be a significant obstacle, and that donations would have to be made in California. The value of current agricultural products donated to charitable organizations by farmers is not available. Based on information in the 1998 California Statistical Abstract, total cash receipts for these products sold by farmers in 1996 was nearly \$12.5 billion.

It is projected that for every \$150 million in gross wholesale values claimed by farmers in contributions, the revenue loss would be around \$5 million. Since this bill lacks definitions, donated products could represent prior year inventory, in some cases, and current year production of comparable or lesser quality that is not readily marketable and may have no wholesale market value. Farmers with operating losses for the year could provide for carryover credits for subsequent years.

The order of magnitude loss could be as high as \$10 million annually (approximately \$300 million in claimed wholesale values) beginning in 1999/2000.

BOARD POSITION

Pending.